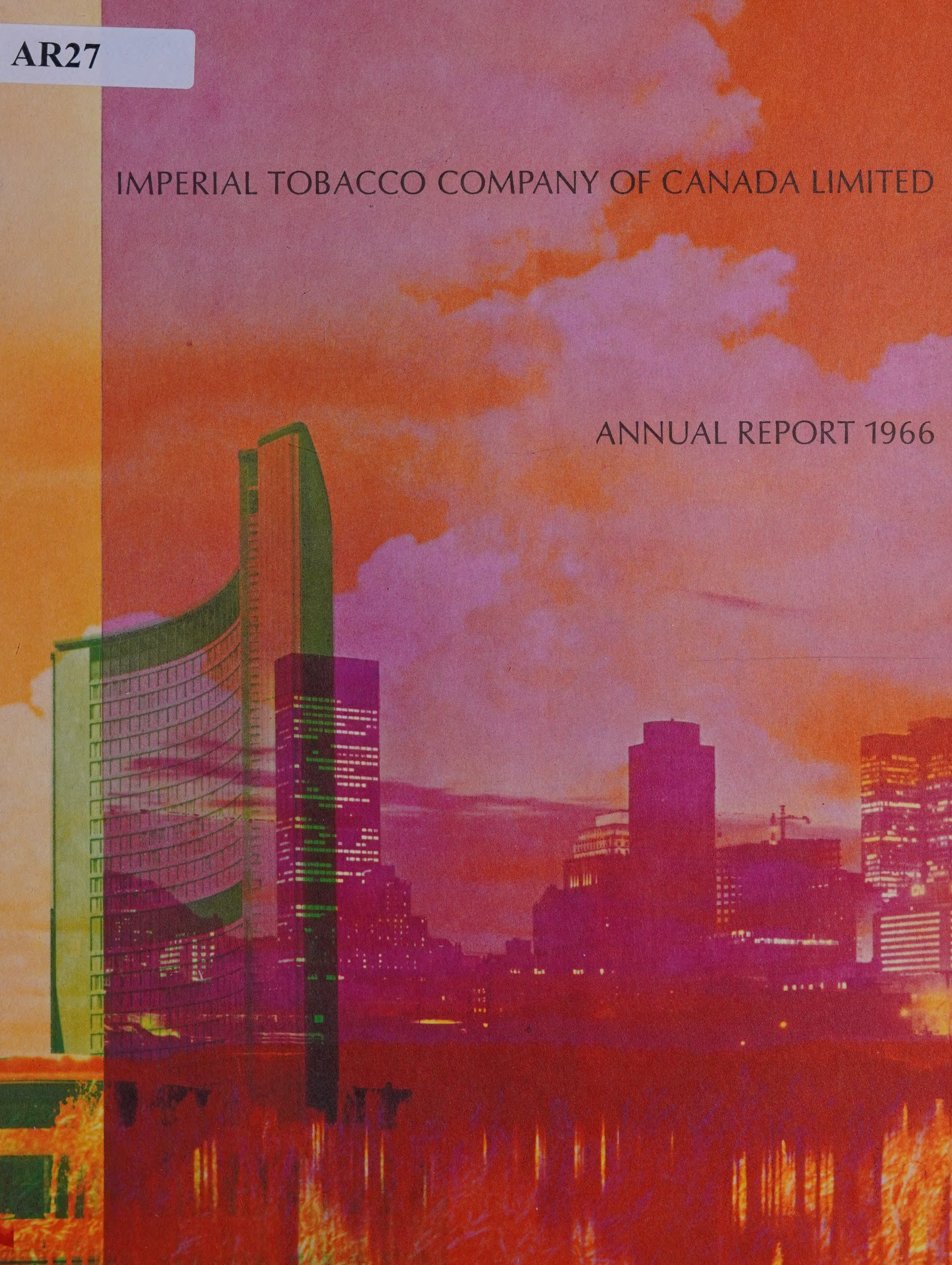
IMPERIAL TOBACCO COMPANY OF CANADA LIMITED

ANNUAL REPORT 1966



OUR COVER THEME *At the dawn of our second century, this mosaic of modern Canada suggests that "we should have unbounded confidence in our collective capacity to continue to build a better life for all Canadians."*

IMPERIAL TOBACCO COMPANY OF CANADA LIMITED

FIFTY-FIFTH ANNUAL REPORT 1966

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THE YEAR AT A GLANCE

CONSOLIDATED NET EARNINGS	
amount for year	$12,725,000
compared to previous year — decrease	606,000
INCOME TAXES	
amount for year	11,314,000
compared to previous year — decrease	1,146,000
EARNINGS PER COMMON SHARE	
amount for year	1.28
compared to previous year — decrease	.06
INVESTMENTS IN NON-CONSOLIDATED SUBSIDIARIES, INCLUDING LOANS AND ADVANCES	
amount at beginning of year	13,077,000
increase during year	5,893,000
amount at end of year	18,970,000
RETAINED EARNINGS	
amount at beginning of year	47,882,000
added during year	3,836,000
amount at end of year	51,718,000
WORKING CAPITAL	
amount at beginning of year	87,421,000
decrease during year	2,815,000
amount at end of year	84,606,000
DIVIDENDS	
amount for year on	
6% cumulative preference shares	394,000
common shares (rate per share 80¢)	7,736,000
all shares	8,130,000

The figures set out on this page provide a quick glance at the results for the year 1966. More comprehensive information appears on pages 21 to 28.

John M. Keith (centre), president, and W. H. Booth (right), elected a director and appointed vice-president, finance, in 1966, examine new home of the Research and Development and the Engineering Departments which neared completion at year-end. Leo C. Laporte, a director of the Company and vice-president, research and development, describes the new facilities. The Company's research program, unique in Canada, compares with the most advanced among tobacco companies in the world.

HIGHER SALES BUT COST-PRICE SQUEEZE DOMINATES YEAR

TOTAL consolidated sales of Imperial Tobacco in 1966 continued to increase, reaching $372,918,000. While sales increased by $6,656,000 over the previous year, net earnings at $12,725,000 were $606,000 lower. These results graphically summarize the cost-price struggle that dominated the year.

Dividends on common shares totalled 80 cents per share for 1966, maintaining the increase of 7½ cents per share initiated the previous year. Since its incorporation in 1912, the Company has paid dividends without

interruption, a record achieved by only a few other companies in North America.

The strongest pull in the cost-price tug-of-war was the sharp rise in cost of leaf tobacco. The flue-cured leaf tobacco of southern Ontario, from which almost all Canadian cigarettes are made, advanced more than 16% in price for the 1965 crop over the 1964 crop. The price for the 1966 crop, which is still being sold, has to date advanced a further 11%.

Aggravating the situation, and contributing to the pressure on auction prices, was the shortage of leaf tobacco. The minimum requirement for domestic and overseas needs had been estimated at 228 million pounds for 1966, but the actual crop was short by some 20 million pounds. Record demand from overseas buyers, primarily due to the Rhodesian situation, cut further into the available supply.

The Marketing Board for the Ontario growers of flue-cured leaf tobacco has given indications that it will allot increased acreage on the basis of a more realistic view of yield-per-acre for the planting of the 1967 crop.

Also tugging at costs were higher wage rates that came into effect during the year in the second stage of the Company's three-year labor agreement. Salaries and fringe benefits advanced as well.

Added revenues from the increased volume of cigarette sales to some extent helped offset rising costs. This was not sufficient to balance the increased costs, so that an increase in the price of cigarettes to our distributors, averaging 2.4 per cent, was announced last August. A price increase in cigars, the first in 17 years, was introduced early in 1966.

Further boosts to costs in 1967 so far have been the unexpected rise in leaf tobacco prices and the increase in Federal sales tax from 11 per cent to 12 per cent at the start of the new year. The latter amounts to a 9 per cent increase in the rate of this sales tax and will cost the Company more than $2,000,000 extra during the year.

Inevitably, the total impact of all these added costs forced a further price increase on cigarettes and certain other tobacco products, but not on cigars, snuff and cigarette papers. The announcement was made by Imperial Tobacco on February 13, 1967 and was followed by an advertisement in Canadian daily and financial newspapers to explain clearly the factors that made the price increase unavoidable.

While the push and pull to hold the line on prices absorbs so much of the Company's attention, the price the smoker has to pay is overwhelmingly affected by the disproportionately heavy federal excise levies on tobacco products. As an example, on a package of 25 cigarettes, the federal tax alone is more than 25 cents. Provincial taxes are in addition, to the point that in some provinces the total amount of federal and provincial taxes is substantially more than half of the retail selling price.

The upward trend in cigarette sales is expected to continue during 1967. Cigar volume was down in 1966, largely attributed to the undue impact of the provincial tax on the small cigarillos in some provinces following the price increase. The long term upward trend in cigar sales should resume in 1967. More information about product sales is provided in the section "Marketing Gains New Momentum" that follows.

In the continuing battle to maintain efficiency, a decision was taken last year to concentrate all the Ontario cigarette-making operations at the Guelph plant and gradually phase out production at the Hamilton plant.

As publicly announced in September, the Hamilton plant, more than 75 years old, had become uneconomic to maintain and operate; it lacks a railway siding and its multi-storey construction does not lend itself to further modernization. The plant in Guelph is only seven years old and is recognized as one of the most up-to-date and progressive cigarette manufacturing plants in the world.

All female plant employees in Hamilton and most of the men have the opportunity of alternative employment at the same rates of pay in Guelph, along with provision for moving costs. Some older employees were offered their pensions ahead of normal retirement. For those leaving the Company separation allowances are being paid along with retraining opportunities and placement assistance.

In recent years the Company has developed a training and education program designed to help employees prepare themselves for better jobs in the future. A further step was taken in 1966 by which employees can complete elementary and secondary school in in-plant classrooms. The Departments of Education of Quebec and Ontario have approved the program and are paying the teachers' salaries. The Company is supplying the textbooks and providing the classrooms.

Imperial Tobacco for some years has been offering a training program for skill development as well as educational assistance programs, in which the scope was widened and financial help increased during the past year.

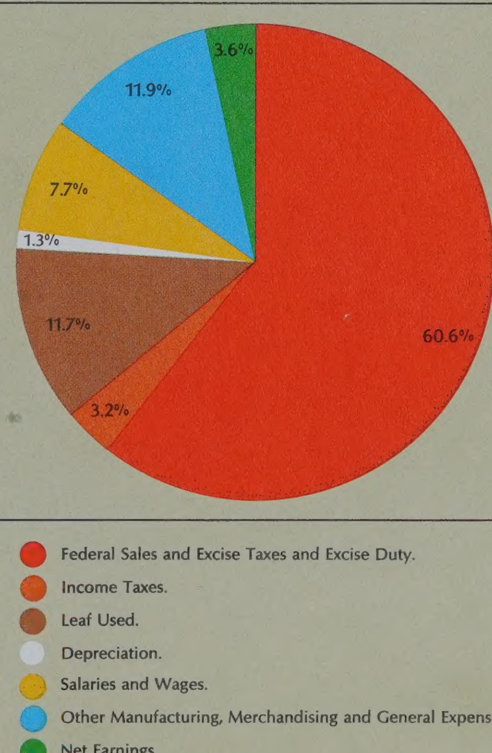
The work of the Company's joint committee of management and union representatives is setting meaningful patterns in dealing with the effects of technological improvements on the employees.

The problems of job competence and job satisfaction at all levels have increasingly engrossed the Company's attention. Of course, they are of concern to all Canadians. The capacity to compete in the world about us can only be met by being qualified to perform effectively in the world of tomorrow.

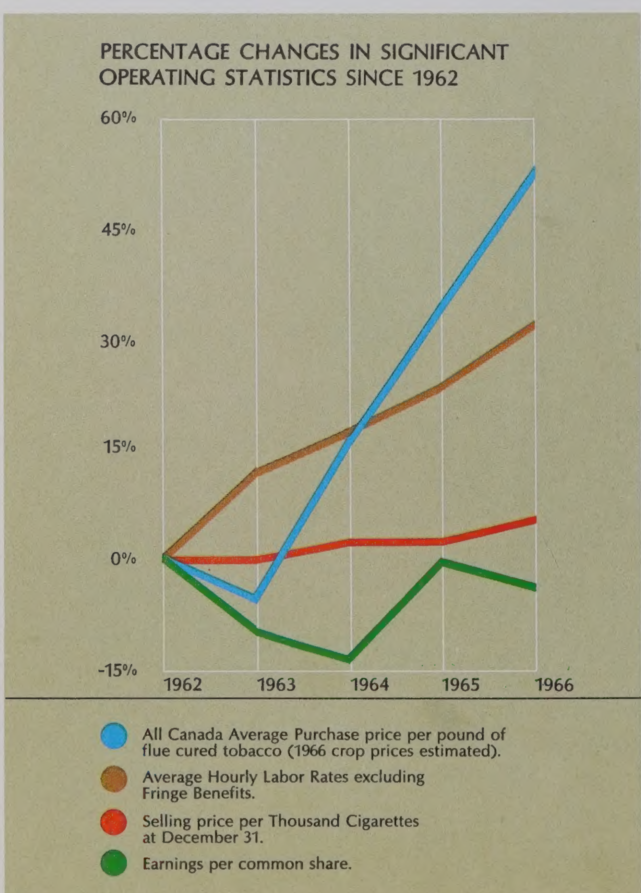
The world of tomorrow is Canada's second century. If we consider but briefly the conditions and problems and worries facing the people of this great country a century ago, we should have unbounded confidence in our collective capacity to continue to build a better life for all Canadians.

(continued on page 7)

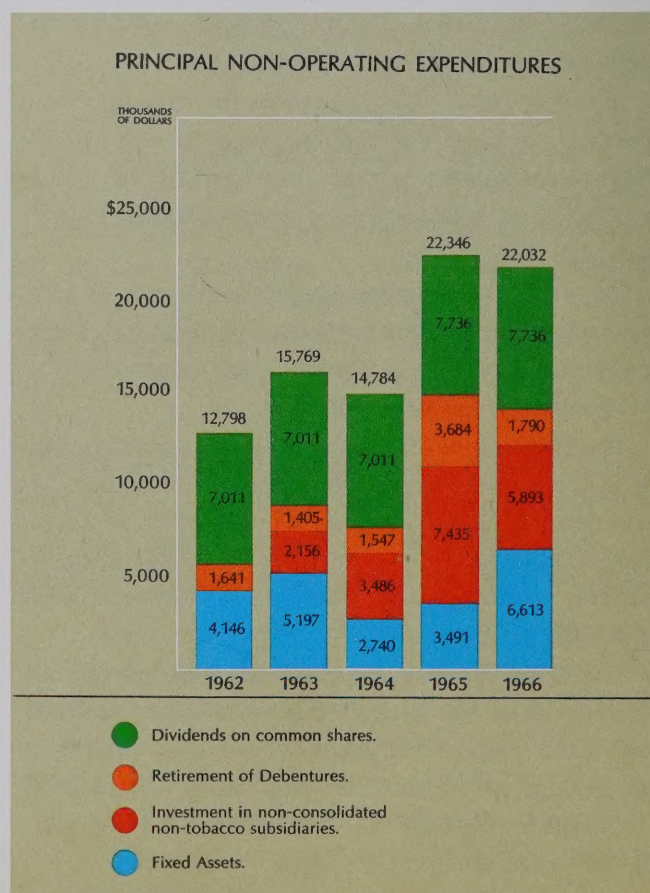
DISTRIBUTION OF 1966 SALES DOLLAR
FROM TOBACCO BUSINESS
EXCLUDING RETAIL OPERATIONS



The cost-price squeeze faced by Imperial Tobacco is clearly shown here. The cigarette price increases were made in the second half of 1964 and 1966 so that the impact on earnings for a full year is not reflected until the succeeding period.



The non-operating cash outlays of the Company have varied from a low of $12,798,000 in 1962 to a high of $22,346,000 in 1965. Investments in non-consolidated subsidiaries include investments prior to them becoming subsidiaries in 1965.



Paul Paré (centre), executive vice-president, tobacco group, and D. E. Kearney (left), vice-president, leaf tobacco, are shown the new "slit-end fold" style of foil carton that eliminates the separate stage of attaching end-labels. Peter Austin, general production manager, describes machinery which was converted by the engineering staff to achieve a saving in cost and added efficiency.

(continued from page 5)

Never has building for the future within Imperial Tobacco been more active. New approaches to organization, to planning, to almost every function are being implemented.

Among senior appointments in 1966, W. H. Booth, formerly treasurer, was elected a director of the Company and named vice-president, finance. Paul Paré, a director of the Company and formerly vice-president, marketing, was named executive vice-president, tobacco group. J. A. Calder, executive vice-president, diversification group, is now devoting his complete energies to these interests, about which a report begins on page 13.

As part of the Company's program to provide more information about its activities, a six-month report to shareholders was issued during the past year for the first time. As well, this Annual Report introduces a number of informative charts.

In the difficult and demanding business conditions of today, our employees are contributing unstintingly. The Board of Directors is most appreciative of their loyalty, devotion and diligence.

In every area of its operations the Company is concentrating its efforts toward more effective results. We are looking to increased sales, which we hope will produce increased earnings in the year ahead.

On behalf of the Board of Directors,

John M. Keith
President

Montreal, 20th February 1967.

MARKETING GAINS NEW MOMENTUM

Christl Haas of Austria, overall champion in the women's division of the 1966 du Maurier International, accepts the du Maurier Cup from L. E. Ricard, vice-president, Peter Jackson Tobacco Sales Limited. Each year trophies are awarded the men's and women's overall champions and are symbolic of amateur skiing supremacy in Canada.

MANUFACTURERS in the tobacco industry, as in many other industries, are facing the need to satisfy rapidly changing and increasingly varied tastes of consumers. This has led to the splintering of once-stable markets and to the development of a greater variety of products.

Imperial Tobacco has taken action to meet this overall challenge and has geared its marketing strategies accordingly. By determining specific objectives, the marketing development team is able to plan more effectively. Through more thorough-going consumer research and information on a particular market's characteristics, earlier and more accurate projections are possible.

Since 1960 the volume of king size cigarettes sold in Canada has increased five-fold. The Company, although late in entering this field, has now secured almost 50% of the king size cigarette market to lead all other manufacturers.

Notable in this group are Matinée, with a sharp increase in sales in 1966; du Maurier, with its wide popularity across Canada; and Peter Jackson, which improved its volume over the jump achieved the previous year.

The popularity of the menthol cigarette has increased steadily each year to a point where its volume has almost tripled that of six years ago. The Company's Cameo is by far the most dominant brand, accounting for over 50% of all menthol cigarette sales in Canada.

The "slide-and-shell" 25's is a package unique to Canada, as compared with the 20-cigarette pack sold in other countries. But Canadian preference for the larger package is clearly indicated by the swing from 38% of the cigarette market in 1960 to more than 60% in 1966.

Among cigar brands, the success story of the decade has been our Old Port family which has risen from less than 10 million cigars ten years ago to more than 110 million in 1966. One of every four cigars sold in Canada is now an Old Port.

Above: The Player's family of cigarettes has been a dominant name on the Canadian scene since early in the century. Reflecting the changing tastes of smokers, Filter Player's and Player's Kings have been added to the group in recent years.

Upper right: Matinée cigarettes in king size enjoyed considerably larger sales in 1966. The Embassy brand, with its extensive range of gifts for coupons, has wide appeal and Cameo in the growing menthol market leads the field with three times the sale of any other menthol cigarette in Canada.

At right: The popular du Maurier brand is the second largest selling filter cigarette brand in Canada and the Peter Jackson brand, in its distinctive package, has been one of the most successful new entries on the market in recent years.

Important additions to the family are the Old Port Tipped and the Old Port Rapier, a long and lean cigar. The first appearance of cigars in vending machines in Canada has been the Old Port Vend Pack, which is expected to make considerable headway in the coming year.

The many shapes in the House of Lords group account for the greatest share of the moderate to higher priced cigars. A distinctive House of Lords Centennial cigar is being introduced this special year. It is a Royal Corona size and is illustrated on the inside back cover of this report.

In pipe tobaccos the most significant development for the Company was the introduction of the Old Port pipe tobacco in the Ontario market. Carefully developed and tested, this Old Port flavor had immediate appeal for pipe smokers.

The popularity of Dutch type tobaccos remains high and the Company's Hollandia brands enjoyed larger sales. Hollandia Aromatic, introduced in 1965, made headway as it gained national distribution. The long-established Old Chum pipe tobacco maintained its important share of the market.

The "roll-your-own" smokers, while becoming fewer each year, are still a large number and require continuing attention to satisfy their changing tastes. Among fine cut tobaccos the new Embassy fine cut is doing well and the Matinée fine cut is also making progress.

The Company supplies most of the snuff and chewing tobaccos sold in Canada. These products are particularly popular with people engaged in woodlands operations, mining, farming and fishing.

The advertising and promotional activities in support of the different product groups and brands are virtually legion. The du Maurier International ski event, with championship races on successive weekends in western and eastern Canada, has attracted men and women skiers of renown from many countries.

Sports car racing has had an increasing appeal and the "Player's" trophy events are highlights of the season across Canada. A milestone will be reached in 1967 with the first Formula 1 race, for more powerful cars, ever held in this country.

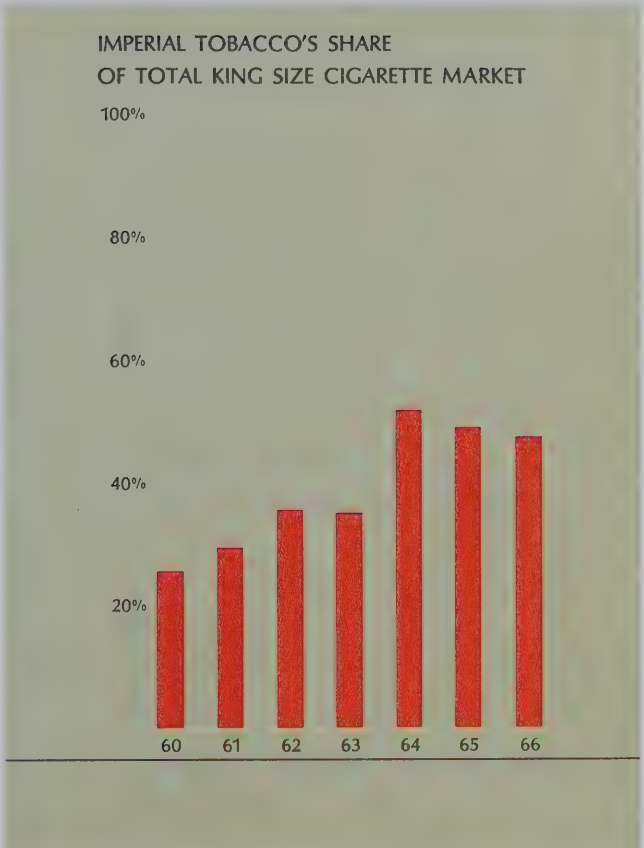
An attractive auxiliary activity has been in women's fashion shows. The Player's "World of Fashion", design-

About half of all the cigars sold in Canada come from General Cigar Company, Limited, the cigar manufacturing subsidiary of Imperial Tobacco. The Old Port family of brands, with its leadership in the large-volume cigarillo market, accounts for one of every four cigars sold in Canada and is exported to various countries. House of Lords is the prestige name among cigars while White Owl, Marguerite and Tiparillo by Robt. Burns have sizeable followings.

1
In six years the market for king size cigarettes has increased by 500%. In this period Imperial Tobacco's brands have doubled this growth rate, moving from one quarter to one half of the total market, to lead all other manufacturers.

2
By the end of 1966 the Old Port share of the total cigar market had grown to 24%, as graphically illustrated here. The rise in sales of Old Port cigars has been spectacular, from less than 10 million ten years ago to 110 million last year.

3
Menthol cigarette sales have increased by almost 300% in the last six years while their share of the market has doubled. Cameo is by far the most popular, accounting for more than half of all menthol cigarettes sold in Canada.



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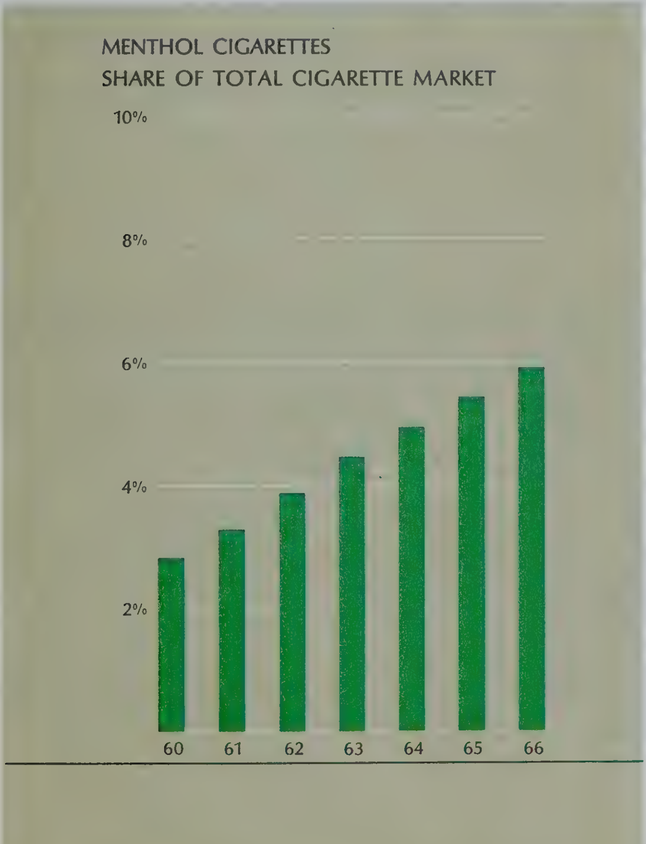

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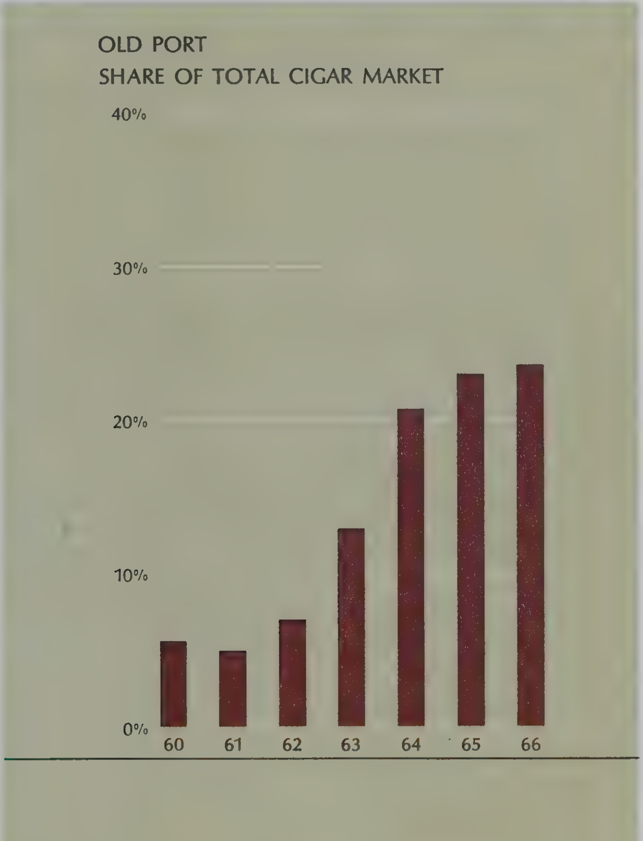


2

In pipe tobaccos, the distinctive new Old Port brand has been added to the well-established Old Chum and Hollandia brands. While fewer smokers roll their own cigarettes, some half-million people in Canada still do. Many enjoy the newer Matinée and Embassy brands of fine cut tobaccos.

ed by the leading couturiers of Canada for Player's, recently received the coveted Judy Award for its "outstanding contribution" to the promotion of Canadian fabrics. As well, special "mobile" fashion shows were presented last spring and summer in the main centres across Canada. The spirit of the Player's sport car races was reflected in the fashion display "which captures all the glamor and exuberance of both racing and race-watching."

A new and developing sport was given a push in 1966 with the first "Player's World" snowmobile championships at Barrie, Ontario. Under the sanction of the International Snowmobile Association, Player's offered substantial prizes for three competitions in the two-day meet—speed, slalom and cross-country races. A considerably enlarged world championship event is scheduled by Player's for this March in Montreal.

The marketing initiative of the Company's sales organizations, as indicated by these few examples, is directed "to keep ahead of the game" in the competition in today's markets.

Research staff of Imperial Tobacco prepare material for a pipe tobacco test. The unmarked pouches and questionnaire forms, on table at right, are given to members of the Pipe Smoking Panels. Testing smokers' reactions in this fashion is one of the important stages in marketing new brands.

United Cigar Stores, Limited, an Imperial Tobacco subsidiary, operates more than 200 retail outlets in choice metropolitan locations and shopping centres across Canada. An increased variety of product lines in attractive settings offers convenience shopping for all members of the family.

DEVELOPMENTS IN DIVERSIFICATION

DIVERSIFICATION is an important part of the Company's corporate plans.

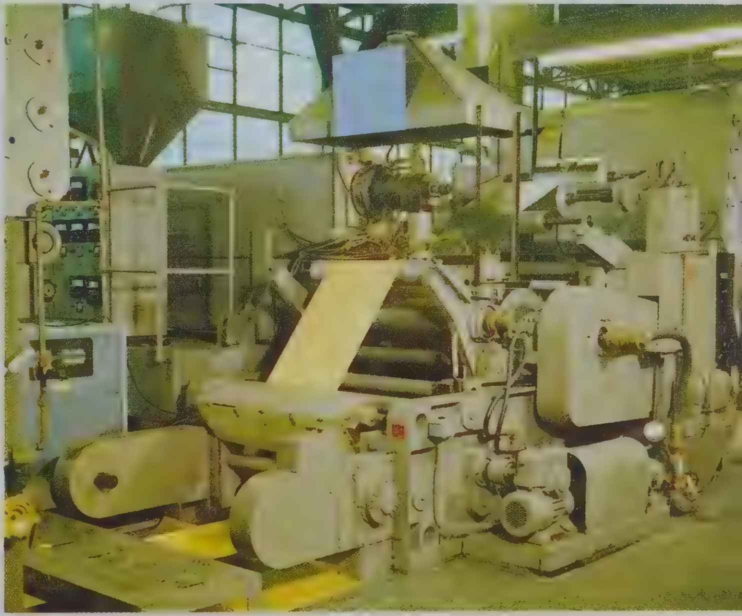
For those enterprises which the Company already owns or controls, the past year was marked by concerted effort toward pre-determined objectives — new plants, new technology, new product lines, new marketing strategies. In some cases, the results are already evident; in others, the build-up is still going on. The profits of Imperial Tobacco should reflect increased contributions from these sources in the years to come.

The search for new enterprises is being systematically conducted by a staff devoted to diversification development, under the full-time direction of an executive vice-president. Strict criteria have been developed for establishing the merits of prospective acquisitions.

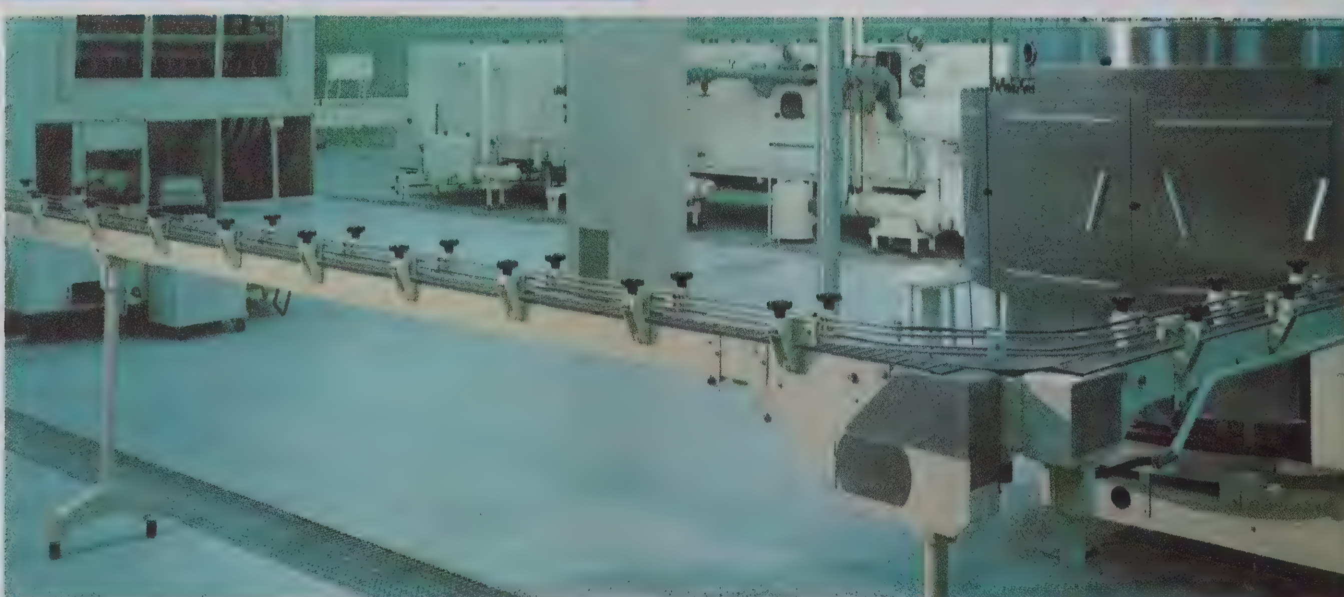
Designed to be one of the most advanced studies in Canadian business history, the program pools many specialized talents and should result in important new undertakings over the years ahead.

See also photographs pages 14 and 15.

Canada Foils, Limited, another Imperial Tobacco subsidiary, is the largest converter in the foil industry in Canada. By the addition last year of this 60-foot long, seven stage, extruder-laminator line, the first designed and built in Canada, the company entered significant new markets.



NEW WINE-MAKING FACILITIES ARE ADDED IN EASTERN AND WESTERN CANADA



Another subsidiary, Beau Chatel Wines Limited (formerly Welland Winery Limited) in Ontario prepared for expansion by putting two new plants into operation in 1966. At top is a view of the stainless steel vats of the new winery at Winona; below, the streamlined bottling plant and warehouse at Rexdale. Both plants are considered among the most modern of the wine industry in North America.

Castle Wines, operated by Growers' Wine Company Limited of British Columbia, in which Imperial Tobacco owns the majority of shares, is developing new grape varieties on the Beau Séjour vineyard in the Okanagan Valley. Castle Wines bought the vineyard last year. The company extended its operations in 1966 by building a new winery at Moose Jaw, Saskatchewan. The attractive design was based on what residents thought a winery should look like. These attractive products of the Moose Jaw winery were also based on the results of consumer research.

Many thousands of visitors to Niagara Falls last year enjoyed the Imperial Tobacco display "Pleasure in the Making" in the new Skylon international centre. Informative exhibits and displays are among the many activities of community service in which the Company participates each year.

RESPONSIBILITIES OF A CORPORATE CITIZEN

THE occasion of Canada's Centennial gave the Company cause to assess — much as any individual might — the part it has played in our country's life and development. Imperial Tobacco has long been conscious of its responsibilities as a corporate citizen.

In fact, the roots of two members of its family go back to before Confederation — B. Houde & Grothé, Limited, based in Quebec City, and The Tuckett Tobacco Company Limited of Hamilton.

A living example of the use of the Company's skills to contribute to the nation's resources is found in the Norfolk county area of southern Ontario. Here, some five short decades ago, only a few hardy farmers attempted to eke out a living on soil that was sandy, barren, and virtually incapable of supporting any vegetation but scrub. This region is now the heartland of Canada's prosperous flue-cured tobacco-growing industry . . . a transformation resulting in large measure from the initiative and leadership of Imperial Tobacco.

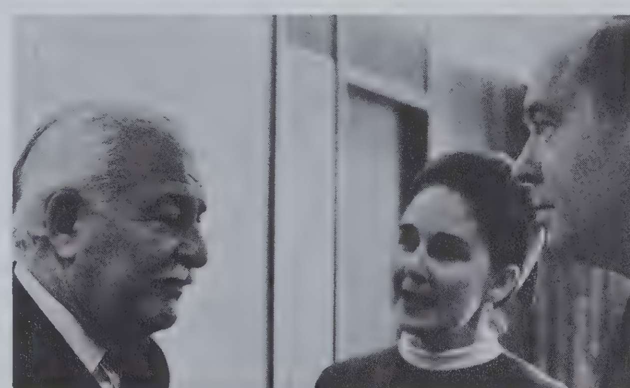
In 1912 virginia type and burley tobaccos were almost all imported; now the tobacco leaf for Canadian cigarettes and other products is almost entirely grown in Canada. The Company, in the early days of the industry, brought experts in growing these types of tobacco from the United States, and, working with the Department of Agriculture, did everything possible to encourage the cultivation of these tobaccos. To help growers keep up with the continuing advances in techniques and equipment, the Company for many years has operated a Practical Experimental Farm, as well as three tree farms.

The importance of this early stimulus and continuing interest is highlighted by the value of the 1966 crops, which will have grossed some $150 million for growers in Ontario, Quebec, Prince Edward Island, Nova Scotia and New Brunswick.

In similar fashion, through the years every effort has been made to develop Canadian sources of supply for

Mayor Jean Drapeau of Montreal cheerfully sprays last section to complete extensive "face-lifting" of plant and offices in Montreal. Looking on (at left) is John M. Keith, president of Imperial Tobacco. The Company seeks to enhance its surroundings at all locations across the country.

Among the educational and community activities the Company supported last year were the Winnipeg Fanfare Concert, a special symphony event in Calgary, and Les Feux Follets, an outstanding folk dancing group. In the upper photo, Arthur Fiedler (left), distinguished guest conductor, talks with Mrs. C. A. E. Jensen, president of the Women's Committee of the Winnipeg Symphony Orchestra, and Bill Smith, Imperial Tobacco's district manager for Manitoba at the time. In the lower photo, the dancers of Les Feux Follets — now on national tour — perform a lively Western number in its program of tributes to the peoples of Canada.



all materials used by the Company. Some 30 years ago Imperial Tobacco pioneered with a paper manufacturer in the production of cigarette paper and cigarette paper booklets in Canada. Other Canadian cigarette manufacturers have followed in directing business to Canadian paper makers.

In the early days of the rapid development of filter-tipped cigarettes, all of the cellulose acetate tow used by the industry had to be imported from the United States. By encouraging and working with Canadian suppliers, Imperial is now able to purchase all its tow in Canada. In many other items the same progress has been made so that today some 95% of all the Company's supply purchases are made in Canada.

In technological research and design, Imperial Tobacco's success has been spectacular. The Company's development engineers have designed or modified machinery that has replaced much of the imported equipment used in the primary stages of processing

The panel of distinguished judges deliberated long and hard to determine the ten finalists for the idea competition "Canada — 2000 A.D.", sponsored as a Centennial project by Imperial Tobacco. They are, from left, Claude Ryan, editor and publisher of Le Devoir *in Montreal; Earle Birney, novelist and poet of British Columbia and presently Writer-in-Residence, University of Toronto; Dr. John J. Deutsch, chairman of the Economic Council of Canada who served as chairman of judges panel; Professor Peter Waite, head of department of history, Dalhousie University; The Hon. Alfred Monnin, Justice of Manitoba Court of Appeal.*

leaf tobacco. In fact, some of this machinery has been widely accepted throughout the world and is now manufactured under licence in a number of other countries, with revenue accruing to the Company in Canada. In Montreal, the Company has had the only significant research and development laboratories in the Canadian tobacco industry. These have been considerably enlarged in 1966, for an outlay of $1,600,000, and promise to make a further substantial contribution to the Company, to the Canadian industry, and to world tobacco technology.

The Company's pricing policy has always been directed toward a fair and reasonable return while making every effort to keep the price of its products as low as possible to the consumer, as illustrated earlier (in chart on page 6). This policy could only be sustained by improvements and technological advances, which have been most capably achieved by the technical and manufacturing staffs.

The Company's policies in training programs and promotions have been designed to encourage initiative and achievement. Procedures for staff training, educational improvement and executive development are probably among the most comprehensive in Canada today.

Over the years Imperial Tobacco has taken a very active part in Canadian business and community service. In the last 25 years the Company has provided three presidents of the Canadian Manufacturers Association and two chairmen of the executive committee of the Canadian Chamber of Commerce. Many other employees have been, and are, actively engaged in all levels of civic, trade, educational and welfare associations across the country.

In the burgeoning cultural field in Canada, the Company has been encouraging an increasing number of local and national efforts. Most recently, on January 29, Imperial Tobacco sponsored the notable two-hour color telecast of Shakespeare's Henry V, performed by the Stratford Festival Company on the CTV network. The Company's decision to forgo the usual commercial breaks in order to avoid interrupting the performance has attracted widespread favorable comment.

CENTENNIAL COMPETITION: "CANADA — 2000 A.D."

THE Centennial idea competition on the future of Canada, sponsored by Imperial Tobacco, attracted a nationwide response far in excess of expectation.

The first stage of "Canada — 2000 A.D." concluded last October 31 with the naming of the 10 finalists. Each received a cheque for $1,500, with a similar amount to follow upon completion of the manuscript in book form by September 1, 1967.

The winner of the Grand Award will be announced at the end of October and will receive a cheque for $30,000, bringing his total prize money to $33,000. The total of $60,000 in award money represents the largest prize for creative writing in Canadian history.

When the brochures announcing the unique idea competition were first sent throughout Canada and to many parts of the world, John M. Keith, president of Imperial Tobacco, expressed "the hope that 'Canada — 2000 A.D.' will furnish a challenge to many hundreds

of thoughtful Canadians . . . perhaps new and exciting ideas may come to light . . .

"The objective is to make a significant, original contribution to the present and future of Canada by encouraging many Canadians to put into black and white how this nation may or should develop over the next 33 years. If it uncovers a useful plan, portrait or prophecy about our future we shall feel well rewarded."

The Company does feel well rewarded.

No writer of novels, no author of the most far-fetched science-fiction story, could have outdone the literally fantastic variety of ideas which emerged from the entries. Neither would any publisher have imagined such a harvest of manuscripts.

More than 1,000 Canadians submitted outlines for a book in English or French from every part of the country, as well as from the United States, England and Europe. The unprecedented response came from people in every walk of life, in every age group from 12 to 91, amateurs and professionals. Their 2,500-word outline projections covered virtually every conceivable aspect of the social, moral, cultural, educational, philosophical, scientific, economic and political life of the country.

Dr. John Deutsch, chairman of the Economic Council of Canada who served as chairman of the five-man judges' panel, reported that "my colleagues and I were profoundly impressed by the originality and imagination revealed in the submissions of many participants. If the completed manuscripts reflect the promise contained in these outlines they may well prove to be valuable additions to Canadian letters."

By and large, the quality of the submissions was of a high order and the prevailing tone exuded a spirit of optimism and great confidence in Canada.

Many of the submissions came from newcomers to our country. In a touching passage of an accompanying letter, a teacher from Halifax wrote: "We are happy new Canadians, and very grateful ones. How I would long to do something of lasting value for Canada . . . I am proud to be a Canadian."

"Sun Acre" is a one-acre artificial island in the heart of the "Man the Provider" agricultural exhibit at Expo 67 which opens in Montreal April 28. Sponsored by the five leading Canadian tobacco manufacturers, Sun Acre will dramatize man's dependence on the sun as the source of life-giving energy for plant growth. This keynote section of the agricultural exhibit, besides showing the cycle of growth and sample crops, will permit visitors to rest and relax in a parklike setting. It is located on Ile Notre Dame, close to the pulp and paper and the Russian pavilions and conveniently reached from Expo's internal transit lines.

DIRECTORS:

JOHN M. KEITH, *president*

J. A. CALDER, *executive vice-president, diversification group*

PAUL PARÉ, *executive vice-president, tobacco group*

WILLIAM H. BOOTH, *vice-president, finance*

BERNARD DANSEREAU, Q.C., *general counsel and secretary*

T. E. R. HAWKINS, *vice-president, administration*

D. EDWARD KEARNEY, *vice-president, leaf tobacco*

R. B. B. LANSDOWN, *vice-president, manufacturing*

LEO C. LAPORTE, *vice-president, research and development*

A. REID TILLEY, *vice-president, corporate planning*

MATTHEWS GLEZOS, *treasurer*

R. A. HILLHOUSE, *comptroller, computer centre and office systems*

G. G. ROSS, *comptroller, accounting*

PIERRE ROBERGE, *assistant secretary*

DELOITTE, PLENDER, HASKINS & SELLS, *auditors*

TOUCHE, ROSS, BAILEY & SMART, *accounting consultants*

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Registrars

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Stock Exchange Listings

Montreal, Toronto, Vancouver and London, England

COMMENTS ON THE YEAR'S OPERATIONS

CONSOLIDATED EARNINGS

Consolidated net sales at $372,918,000 increased by $6,656,000 or about 2%. Cigarette sales exceeded this rate of increase by a considerable margin due to higher volume and a price increase that went into effect 29th August 1966, but sales of fine cut and pipe tobaccos, cigars and leaf tobacco declined.

In order to give more information about the Company's operations, federal sales and excise taxes and excise duty, which are paid directly to the Federal Government, have been shown separately for the first time. It should be noted that additional taxes on our products, not included in the net sales figures, are collected at the consumer level by all Provinces except one.

Despite the increase in sales, net earnings at $12,725,000 showed a decrease of $606,000 or about 5%. After dividends on preference shares, earnings per common share were $1.28, down from $1.34 in 1965. The main factor was the substantially higher cost of leaf referred to in the President's report and illustrated in the graph on page 6. Increased salaries, wage rates and prices for other goods and services also contributed to the drop in earnings. Income from investments in non-consolidated subsidiaries showed an increase of $235,000, mainly due to dividends in 1966 on Canada Foils, Limited shares purchased near the end of 1965. There was a reduction in interest on funded debt of $113,000 due to the 2⅞% debentures having matured on 15th April 1966, and the elimination of interest charges in 1966 on debentures redeemed in advance of maturity during 1965.

CONSOLIDATED RETAINED EARNINGS

A transfer of $749,000 was made to accumulated depreciation to provide for the additional depreciation requirement arising out of the increased replacement value of fixed assets as at 31st December 1966. A charge of $269,000 resulted from the net loss on disposal of fixed assets, and the capital increment of $575,000 applicable to these disposals was transferred to retained earnings.

During the year, 51,038 of the 6% cumulative preference shares were purchased and cancelled. The premium, brokerage and tax on these shares, amounting to $68,000, was charged to retained earnings and $248,000, representing the par value of the cancelled shares, was transferred to capital surplus.

Regular dividends were paid during the year on outstanding 6% cumulative preference shares. A final dividend for 1966 of 10¢ per common share has been declared payable 31st March 1967, making total dividends of 80¢ per common share for the year. This is the same as the aggregate amount paid for 1965 when total common dividends for the year were increased by 7½¢ per share over the amount paid for each of the four previous years. For 1966 however, a higher proportion of the total distribution was paid by way of interims during the year in line with the policy announced in November 1965.

Consolidated retained earnings at 31st December 1966 showed an increase of $3,836,000 over 1965.

BALANCE SHEET

Working capital decreased by $2,815,000 as explained in detail in the statement of changes in consolidated working capital. Apart from dividends, the main withdrawals from working capital were $6,613,000 for expenditures on fixed assets and $5,893,000 for investments in non-consolidated subsidiaries, including loans and advances, in respect of Canada Foils, Limited, Growers' Wine Company Limited and Beau Chatel Wines Limited (formerly Welland Winery Limited).

Fixed assets were again revalued at replacement cost as at 31st December 1966, and as a result capital increment increased by $909,000. This increase would have been greater if cognizance had not been taken of a reduction, effective 1st April 1967, in the rate of sales tax on production machinery. Because the reduction was both imminent and material, it was thought proper to take it into account when computing replacement cost as at 31st December 1966.

GENERAL

Following declaration of the final dividend on common shares for 1966, the first interim for 1967 of 17½¢ per share was declared payable 31st March 1967.

IMPERIAL TOBACCO COMPANY OF CANADA LIMITED and Subsidiary Companies
Year ended 31st December 1966 with comparative figures for 1965

CONSOLIDATED EARNINGS (note 1)

	1966	*1965*
Net sales	$372,918,000	$366,262,000
Federal sales and excise taxes and excise duty	212,401,000	209,495,000
Manufacturing costs, merchandising and general expenses (note 2)	133,486,000	127,980,000
Depreciation (note 3)	4,802,000	4,539,000
Total cost of operations	350,689,000	342,014,000
Earnings from operations	22,229,000	24,248,000
Income from investments in non-consolidated subsidiaries (note 1)	336,000	101,000
Income from other investments	1,557,000	1,638,000
	24,122,000	25,987,000
Interest on funded debt	83,000	196,000
Earnings before income taxes	24,039,000	25,791,000
Income taxes (note 4)	11,314,000	12,460,000
Net earnings for the year	$ 12,725,000	$ 13,331,000

CONSOLIDATED RETAINED EARNINGS (note 1)

Retained earnings 1st January	$ 47,882,000	$ 45,570,000
Net earnings for the year	12,725,000	13,331,000
Additional depreciation requirement (note 3)	*749,000*	*3,011,000*
Net loss on disposal of fixed assets	*269,000*	*148,000*
Capital increment applicable to disposal of fixed assets	575,000	892,000
Premium, brokerage and tax on 6% cumulative preference shares purchased	*68,000*	*74,000*
Transferred to capital surplus (note 8)	*248,000*	*207,000*
Write-off of goodwill arising from acquisition of a consolidated subsidiary	—	*322,000*
	59,848,000	56,031,000
Dividends (note 5)	8,130,000	8,149,000
Retained earnings 31st December	$ 51,718,000	$ 47,882,000

The notes on pages 23 and 24 form an integral part of these statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. *Principles of consolidation and related information*

The consolidated financial statements include the accounts of Imperial Tobacco Company of Canada Limited and all subsidiary companies except Canada Foils, Limited, Growers' Wine Company Limited and Beau Chatel Wines Limited (formerly Welland Winery Limited). It is considered impractical at this time to consolidate these latter subsidiaries.

The earnings of non-consolidated subsidiaries have been included in the consolidated accounts only to the extent of dividends received.

In respect to non-consolidated subsidiaries, the company's proportion of (a) the net loss for fiscal periods ended in 1966 amounted to $25,000 and (b) the net decrease in retained earnings since acquisition to 31st December 1966 amounted to $215,000 for which a provision has been set aside in consolidated retained earnings.

2. *Manufacturing costs, merchandising and general expenses*

Included in this item is the amount of $513,000 (1965 — $380,000) for total remuneration paid to directors, all of whom were employed as full-time officers of the company.

3. *Fixed assets and depreciation*

a) Depreciation charged against earnings for the year and accumulated depreciation to date are based on replacement cost both in the consolidated statements and in the books of the individual companies. The same rates applied to historic costs would have given rise to a charge for the year of $3,768,000 (1965 — $3,486,000) and accumulated to date of $36,932,000 (1965 — $33,891,000).

b) Additional depreciation requirement of $749,000 (1965 — $3,011,000) in respect of prior years, arising from current year's increase in replacement cost, has been charged to retained earnings.

c) Fixed assets are recorded in the books of the companies at historic cost and are shown at replacement cost only on consolidation.

d) The replacement cost of fixed assets is based on appraisals made as at 31st December. For 1966 buildings were appraised at replacement cost and land at current market value by Canadian Appraisal Company Limited. Machinery and equipment were valued at replacement cost by company officials utilizing price indexes obtained from the Dominion Bureau of Statistics and, where necessary, price indexes based on government and industry studies in other countries. On consolidation the use of replacement cost gives rise to an increase in fixed assets before depreciation of $39,795,000 (1965 — $38,886,000) which is reflected in capital increment.

e) The effects of the foregoing are summarized as follows:

	1966	*1965*
Land, buildings and equipment at historic cost	$ 72,557,000	$ 67,076,000
Capital increment	39,795,000	38,886,000
Replacement cost	112,352,000	105,962,000
Less:		
Accumulated depreciation 1st January	61,905,000	55,880,000
Accumulated depreciation on disposals during year	*1,166,000*	*1,525,000*
Depreciation for the year	4,802,000	4,539,000
Additional depreciation requirement transferred from retained earnings	749,000	3,011,000
Accumulated depreciation based on replacement cost	66,290,000	61,905,000
Fixed assets	$ 46,062,000	$ 44,057,000

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. *Income taxes*

The charge for income taxes exceeds the amount payable by $704,000 (1965 — the reverse by $101,000) as a consequence of allowable depreciation being more (1965 — less) than the amount charged in the accounts. Since the reverse is expected to occur in some future years, the amount concerned is included in the balance sheet item termed "Accumulated income tax reductions applicable to future years".

5. *Dividends*

	1966	*1965*
Dividends of Imperial Tobacco Company of Canada Limited:		
On 6% cumulative preference shares	$ 394,000	$ 413,000
On common shares:		
Four interim dividends totalling 70 cents per share (1965 — 62½ cents)	6,769,000	6,044,000
Provision for final dividend for year of 10 cents per share (1965 — 17½ cents)	967,000	1,692,000
	$ 8,130,000	$ 8,149,000

6. *Provision for dividends*

Provision for dividends of Imperial Tobacco Company of Canada Limited:

	1966	*1965*
Accrued on preference shares	$ 98,000	$ 101,000
Final for year on common shares	967,000	1,692,000
	$ 1,065,000	$ 1,793,000

7. *Paid up share capital*

		1966	*1965*
6% cumulative preference shares par value $4.86⅔ each			
Authorized and issued	1,650,000 shares		
Less purchased and cancelled:			
as at 31st December 1965	259,627 shares		
	1,390,373 shares		$ 6,766,000
during 1966	51,038 shares		
Outstanding 31st December 1966	1,339,335 shares	$ 6,518,000	
Redeemable sinking fund preference shares par value $25 each			
Authorized: 200,000 shares			
Issued: None		—	—
Common shares no par value			
Authorized: 10,800,000 shares			
Issued: 9,670,532 shares		48,353,000	48,353,000
		$54,871,000	$55,119,000

8. *Capital surplus*

The sum of $248,000 (1965 — $207,000) has been transferred from retained earnings and designated as capital surplus arising from cancellation of 51,038 (1965 — 42,405) 6% cumulative preference shares par value $4.86⅔ each.

9. *Trusteed pension plan*

Outstanding commitments in respect of funding of back service of employees under a trusteed pension plan amount to $4,225,000 at 31st December 1966 (1965 — $4,615,000) payable in annual instalments to 1981. The 1966 instalment was $390,000 (1965 — $390,000).

IMPERIAL TOBACCO COMPANY OF CANADA LIMITED and Subsidiary Companies
31st December 1966 with comparative figures for 1965

CONSOLIDATED BALANCE SHEET (note 1)

	1966	1965
CURRENT ASSETS		
Cash and term deposits	$ 11,545,000	$ 11,263,000
Marketable securities (market value $9,800,000; 1965 $11,146,000)	9,741,000	11,122,000
Accounts receivable less allowance for doubtful accounts	16,494,000	16,849,000
Leaf tobacco, manufacturing materials, supplies and merchandise (at average cost)	75,484,000	81,179,000
Total Current Assets	113,264,000	120,413,000
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	9,870,000	8,331,000
Income, excise and other taxes	17,723,000	21,079,000
Provision for dividends (note 6)	1,065,000	1,793,000
2⅞% debentures (matured 15th April 1966)	—	1,789,000
Total Current Liabilities	28,658,000	32,992,000
Working Capital (Net Current Assets)	84,606,000	87,421,000
OTHER ASSETS		
Loans and advances to non-consolidated subsidiaries	1,395,000	786,000
Investments in non-consolidated subsidiaries (at cost)	17,575,000	12,291,000
Other investments (at cost)	951,000	1,061,000
Special refundable tax	540,000	—
Prepaid expenses and deferred charges	1,217,000	1,282,000
Fixed assets (note 3)	46,062,000	44,057,000
Goodwill, trade marks and patents (at nominal value)	1,000	1,000
	152,347,000	146,899,000
OTHER LIABILITIES		
3% sinking fund debentures (maturing 1st March 1970)	2,261,000	2,262,000
Accumulated income tax reductions applicable to future years (note 4)	2,190,000	1,486,000
	4,451,000	3,748,000
Excess of Assets over Liabilities	$147,896,000	$143,151,000
Provided by:		
SHAREHOLDERS' RISK CAPITAL		
Paid up share capital (note 7)	54,871,000	55,119,000
Capital increment (note 3)	39,795,000	38,886,000
Capital surplus (note 8)	1,512,000	1,264,000
Retained earnings (note 1)	51,718,000	47,882,000
	$147,896,000	$143,151,000

Approved by the Board:
JOHN M. KEITH, Director
W. H. BOOTH, Director

The notes on pages 23 and 24 form an integral part of these statements.

STATISTICAL HIGHLIGHTS — TEN YEAR REVIEW

(Thousands of Dollars — except 'per common share' statistics)

	1966	1965	1964	1963	1962
SALES AND EARNINGS					
Net sales (c)	372,918	366,262	351,456	355,065	373,392
Depreciation (d)	4,802	4,539	4,243	4,050	3,757
Earnings before income taxes	24,039	25,791	22,271	23,063	25,594
Income taxes	11,314	12,460	10,765	11,049	12,233
Net earnings	12,725	13,331	11,506	12,014	13,361
Earned on common shares	12,331	12,918	11,083	11,566	12,879
Per common share	$ 1.28	$ 1.34	$ 1.15	$ 1.20	$ 1.33
DIVIDEND RECORD					
On preference shares	394	413	423	448	482
On common shares	7,736	7,736	7,011	7,011	7,011
Per common share	$ .80	$ .80	$ .72½	$ .72½	$ .72½
CAPITAL EXPENDITURES					
On fixed assets	6,613	3,491	2,740	5,197	4,146
FINANCIAL POSITION					
Current assets (e)	113,264	120,413	123,628	121,537	123,127
Current liabilities	28,658	32,992	30,024	28,120	30,048
Working capital	84,606	87,421	93,604	93,417	93,079
Investments in non-consolidated subsidiaries, including loans and advances	18,970	13,077	—	—	—
Fixed assets (before depreciation) (f)	112,352	105,962	99,510	97,688	90,083
Fixed assets (less depreciation) (g)	46,062	44,057	43,630	44,279	42,039
Debentures (h)	2,261	2,262	7,035	8,582	9,987
Excess of assets over liabilities	147,896	143,151	136,535	130,836	125,842
SHAREHOLDERS' RISK CAPITAL					
Equity of preference shareholders	6,518	6,766	6,973	7,215	8,030
Equity of common shareholders	141,378	136,385	129,562	123,621	117,812
Per common share	$14.62	$14.10	$13.40	$12.78	$12.18

(a) 1960 revised in accordance with 1961 and subsequent years' presentation.

(b) 1957/59 revised in accordance with 1961 and subsequent years' presentation to the extent that equity reserves are included under shareholders' risk capital. Effect of replacement cost valuation of fixed assets on yearly charge for depreciation, on fixed assets, on accumulated depreciation and on equity of common shareholders and effect of write down on goodwill not reflected.

(c) Not published for years previous to 1960.

STATISTICAL HIGHLIGHTS — TEN YEAR REVIEW

(Thousands of Dollars — except 'per common share' statistics)

1961	1960(a)	1959(b)	1958(b)	1957(b)	
					SALES AND EARNINGS
359,105	342,775	—	—	—	(c) Net sales
3,482	3,402	4,332	3,871	3,334	(d) Depreciation
26,800	26,177	24,222	21,481	22,595	Earnings before income taxes
12,943	12,557	13,111	10,816	11,641	Income taxes
13,857	13,620	11,111	10,665	10,954	Net earnings
13,375	13,138	10,629	10,183	10,472	Earned on common shares
$ 1.38	$ 1.36	$ 1.10	$ 1.05	$ 1.08	Per common share
					DIVIDEND RECORD
482	482	482	482	482	On preference shares
7,011	6,527	6,527	6,527	6,527	On common shares
$ .72½	$ .67½	$ .67½	$ .67½	$ .67½	Per common share
					CAPITAL EXPENDITURES
4,179	5,645	8,560	8,581	7,787	On fixed assets
					FINANCIAL POSITION
117,590	112,503	108,487	105,731	102,676	(e) Current assets
29,474	30,069	34,174	31,069	27,134	Current liabilities
88,116	82,434	74,313	74,662	75,542	Working capital
—	—	—	—	—	Investments in non-consolidated subsidiaries, including loans and advances
83,411	82,788	54,105	46,927	39,160	(f) Fixed assets (before depreciation)
40,757	41,649	16,628	12,769	8,485	(g) Fixed assets (less depreciation)
11,628	12,796	14,056	15,177	16,217	(h) Debentures
118,058	108,992	108,963	104,135	99,686	Excess of assets over liabilities
					SHAREHOLDERS' RISK CAPITAL
8,030	8,030	8,030	8,030	8,030	Equity of preference shareholders
110,028	100,962	100,933	96,105	91,656	Equity of common shareholders
$11.38	$10.44	$10.44	$ 9.94	$ 9.48	Per common share

(d) 1960/66 based on replacement cost; 1957/59 based on historic cost and including charge for fixed asset replacement.

(e) 1960/62 revised to exclude prepaid expenses and deferred charges.

(f) 1960/66 based on replacement cost; 1957/59 based on historic cost.

(g) 1960/66 net after accumulated depreciation based on replacement cost; 1957/59 net after accumulated depreciation based on historic cost and including fixed asset replacement reserve.

(h) Excluding maturities within twelve months which are reflected in current liabilities.

STATEMENT OF CHANGES IN CONSOLIDATED WORKING CAPITAL during the year ended 31st December 1966

Increased by:		
Net earnings	$12,725,000	
Depreciation	4,802,000	
Prepaid expenses and deferred charges	65,000	
Amount realized on sale of fixed assets	272,000	
Accumulated income tax reductions applicable to future years	704,000	
Other investments	110,000	$18,678,000
Decreased by:		
Expenditures on fixed assets	6,613,000	
Loans and advances to non-consolidated subsidiaries	609,000	
Investments in non-consolidated subsidiaries	5,284,000	
Special refundable tax	540,000	
Dividends	8,130,000	
Purchase of 6% cumulative preference shares	316,000	
Debentures redeemed in advance of maturity	1,000	21,493,000
Net decrease		2,815,000
Working capital at beginning of year		87,421,000
Working capital at end of year		$84,606,000

AUDITORS' REPORT

DELOITTE, PLENDER, HASKINS & SELLS, Chartered Accountants
Sun Life Building, Montreal

To the Shareholders
of Imperial Tobacco Company of Canada Limited

We have examined the consolidated balance sheet of Imperial Tobacco Company of Canada Limited and Subsidiary Companies as at 31st December 1966 and the statements of consolidated earnings and consolidated retained earnings for the year ended on that date. Our examination included a general review of the accounting procedures and such tests of the accounting records and other supporting evidence as we considered necessary in the circumstances except that in the case of certain non-consolidated subsidiary companies we have relied upon the reports of other auditors. Insofar as our opinion expressed below relates to information contained in the financial statements of those companies, it is based solely upon the reports of such other auditors.

In our opinion, the accompanying consolidated balance sheet, which incorporates the adjustment to the values of fixed assets referred to in note 3(c), and statements of consolidated earnings and consolidated retained earnings present fairly the financial position of the companies as at 31st December 1966 and the results of their operations for the year ended on that date, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

We also examined the accompanying statement of changes in consolidated working capital during the year ended 31st December 1966 and the statistical highlights which are presented as supplementary information and, in our opinion, these statements present fairly the information shown therein.

Deloitte, Plender, Haskins & Sells

20th February 1967.

Auditors.

PRINTED IN CANADA

The Royal Corona "Centennial Cigar" by House of Lords.